Australian tax implications for significant global entities and country-by-country reporting entities

Multinational groups with operations in Australia must understand the critical concepts of Significant Global Entity (SGE) and a Country-by-Country Reporting Entity (CbCRE) as these trigger numerous targeted integrity and tax transparency measures, and potentially a draconian penalty regime. Generally, this is targeted at larger groups with global revenues of more than A$1 billion.

The rules do have some intricacies, particularly for some groups with majority private equity ownership, which can find themselves classified as SGEs, but not CbCREs. Careful consideration of these rules is strongly recommended given the very harsh outcomes and incremental obligations they entail.

1. Distinguishing SGEs and CbCREs

Per section 960-555 of the *Income Tax Assessment Act 1997* (ITAA 1997), an entity will be an SGE for an income year or period if it:

- Has annual global income of at least AUD 1 billion;
- Is part of a group of entities consolidated for accounting purposes with annual global income of at least AUD 1 billion; or
- Is a member of a 'notional listed company group' with annual global income of at least AUD 1 billion.

The rules effectively distinguish an SGE from a CbCRE, with a CbCRE effectively being a subset of a SGE. A 'notional listed company group' is, broadly, a group of entities that would be consolidated for accounting purposes if exceptions to consolidation were disregarded. A practical example of this would be the application of the exception to consolidated for 'investment entities' under paragraph 4B of AASB 10 *Consolidated Financial Statements* to entities held by private equity funds.

Per section 815-370 of the ITAA 1997, CbCREs are SGEs, that would remain SGEs if the exceptions to consolidation were applied . Extending from the example above, a private equity fund may be an SGE but not a CbCRE. This is because the exception to consolidation for 'investment entities' under paragraph 4B of AASB 10 would need to be applied for the purpose of assessing whether the entity is a CbCRE, but is disregarded for the purpose of assessing whether the entity is an SGE.

2. SGE Obligations

GEs are subject to the following three measures:

a. Significantly increased penalties
b. Multinational Anti-Avoidance Law (MAAL)
c. Diverted Profits Tax (DPT)

a. Significantly increased penalties

The significant increase of penalties to SGEs represents a significant practical challenge for SGEs. Specifically, the following administrative penalties are doubled for SGEs:

- Making a false or misleading statement
- Making a statement which treats a law as applying in a way that was not reasonably arguable
- Failure to provide a document as required
- Entering into tax avoidance and profit shifting schemes that result in scheme benefits

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Additionally, and critically, failure to lodge on time penalties have been multiplied by up to 500 times – a single late lodgment of 113 days can result in a penalty of up to $910,000 and even a day of delinquency attracts a penalty of $182,000.

Given the harsh penalty regime in place for SGEs, it is important to ensure that you are addressing your Australian tax obligations in a timely manner. FTL penalties apply to all 'approved forms', the definition of which includes, but is not limited to:

- Income Tax returns
- Activity Statements and GST annual returns
- Fringe Benefits Tax returns
- Country by Country reporting statements
- General Purpose Financial Statements (GPFS)
- Single Touch Payroll reports
- PAYG Payment Summary Annual Reports

SGEs should continue to review their internal processes to ensure they remain vigilant with their reporting obligations as the imposition of penalties could pose a serious financial risk.

SGEs should also review their technical positions, assess the reasonableness of their positions, and ensure their transfer pricing documentation is contemporaneous.

Given the intense rules that are applied to SGEs, it is important to advise your tax adviser of your SGE status or work with your tax adviser to determine your SGE status. External advisers often do not have access to the global structure of their clients, and as such it is important to raise this with your tax advisers at the outset if you are concerned about your SGE status. Importantly, any changes in your structure or business operations may result in a change to your SGE status and as such, this should be reviewed on an ongoing basis.

> If you are considered an SGE, or require assistance in establishing your SGE status, it is important that you contact your RSM representative to ensure that your compliance obligations are met.

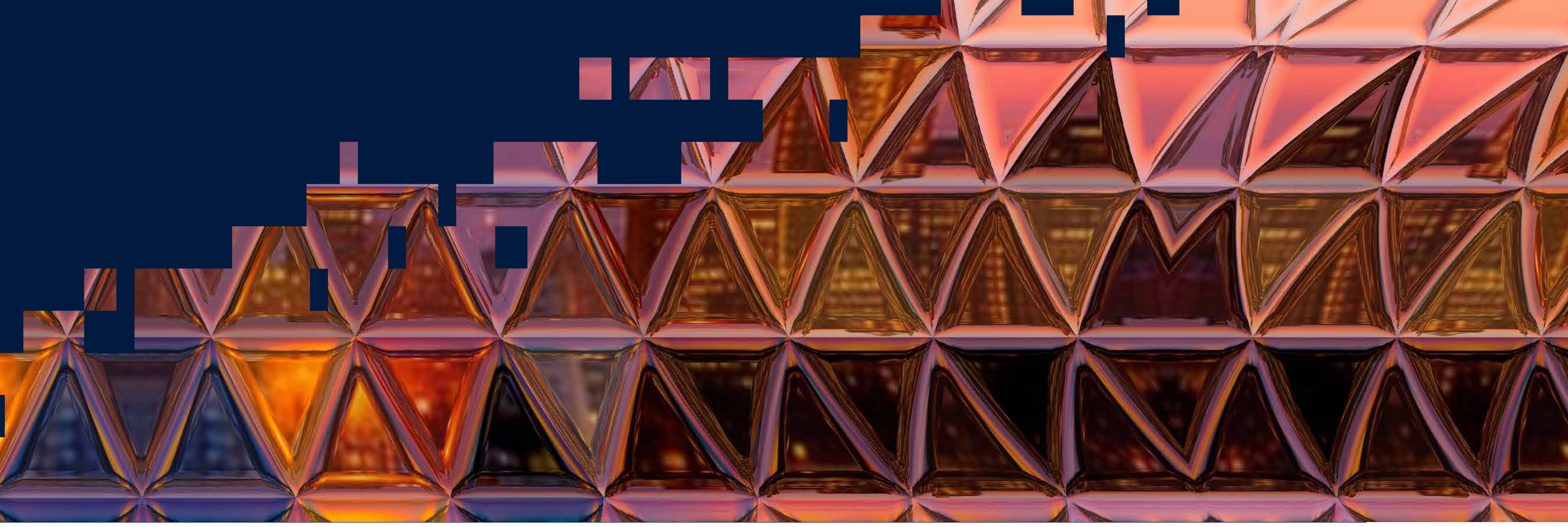
b. MAAL

The MAAL is an anti-avoidance measure which generally applies where:

- A foreign entity supplies goods or services to an Australian customer
- An Australian entity, that is an associate of or is commercially dependent on the foreign entity, undertakes activities directly in connection with the supply
- Some or all of the income derived by the foreign entity is not attributable to an Australian permanent establishment
- The principal purpose, or one of the principal purposes of the scheme is to obtain an Australian tax benefit or to obtain both an Australian and foreign tax benefit

In practice, this is at greatest risk of applying where a multinational group makes supplies directly to Australian customers, with the support of a cost-plus Australian "sales and marketing" entity. The MAAL seeks to ensure that the Australian entity becomes a "buy-sell" entity which is remunerated on an operating margin basis (which will typically be higher than a cost-plus service provider).

The MAAL applies irrespective of when the relevant scheme was entered into and it is not affected by the operation of Australia's double tax agreements, thereby giving rise to the possibility of double taxation.



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c. DPT

The DPT is also an anti-avoidance measure which is imposed at a punitive rate of 40% and was designed to ensure that the tax paid by SGEs properly reflects the economic substance of their activities in Australia. It aims to prevent the diversion of profits offshore through contrived arrangements, broadly being arrangements where non-routine profits are accruing in circumstances where there is insufficient substance to warrant them.

Broadly, the DPT applies if under a scheme, or in connection with a scheme:

- A taxpayer (the "relevant taxpayer") has obtained a tax benefit in connection with the scheme in an income year
- A foreign entity, that is an associate of the relevant taxpayer, entered into or carried out the scheme or is otherwise connected with the scheme
- The principal purpose, or one of the principal purposes of a person who entered into or carried out the scheme, is to enable the relevant taxpayer to obtain an Australian tax benefit or to obtain both an Australian and foreign tax benefit.

There are some exceptions to the DPT's application, namely, the "de minimis" $25 million income test, the sufficient foreign tax test, and the sufficient economic substance test. These should be explored in detail if DPT appears potentially relevant to your business.

The DPT is likewise not affected by the operation of Australia's double tax agreements.

3. CbCRE Obligations

In addition to the general SGE obligations, CbCREs are also subject to the following measures:

- GPFS filing obligations
- CbC Reporting

d. GPFS filing obligations

A corporate tax entity that is also a CbCRE must give GPFS to the Commissioner by the lodgement due date of its income tax return (unless they have already been provided to ASIC by the ASIC filing due date). This is required from the first year of becoming a CbCRE and interestingly, the ATO does not have the power to grant an exemption for any GPFS filings.

The Commissioner will give a copy of the GPFS to the Australian Securities and Investment Commission (ASIC) which will appear on ASIC's register and will be available to the public. This has raised some privacy concerns for multinationals, where this information may not have previously been made public.

This has impacted on a number of smaller Australian entities, which are considered SGE's as they were previously not required to have GPFS prepared. While there is no requirement for these GPFS to be audited, they must comply with the Australian accounting standards or commercially accepted accounting principles (CAAP) so an audit is considered best practice to ensure adherence to the relevant accounting standards. Taxpayers should consider how they will satisfy their GPFS reporting requirements in advance of their year-end to ensure lodgement can be made by the due date and manage any FTL penalties.

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e. CbC Reporting

Where an entity was a CbCRE in the preceding income year, it will also be required to provide three reports to the ATO detailing its global financial activities:

- **The CbC report:** Containing information about where the economic activity is undertaken and profits that are reported by the global group
- **The Master file:** Containing a high-level description of the group's global business operations, including an outline of the group structure as well as intangibles and intercompany financing
- **The Local file:** Containing information about a local entity's management structure and business strategy, cross border related party transactional data, including information about how transfer pricing decisions have been made as well as financial accounts for the Australian entity

> As such, there is often a 1 year "transitional year" provided in respect of the CBC Reporting, though it is important to carefully review the timing (as this does not always apply as expected for some entities i.e. permanent establishments). Generally, an entity has 12 months after year-end to lodge the relevant reports.

Australia has signed the CbC Multilateral Competent Authority Agreement (MCAA) to facilitate the exchange of CbC reports between tax authorities in different jurisdictions. As such, there are some exemptions and concessions that should be explored when considering your CbC reporting requirements.

Summary of requirements

Requirement	SGE only	SGE and CbCRE
a. Significantly increased penalties	✓	✓
b. Multinational Anti-Avoidance Legislation (MAAL)	✓	✓
c. Diverted Profits Tax (DPT)	✓	✓
d. Lodgment of General Purpose Financial Statements with the ATO	×	✓
e. CbC reporting (CbC Report notification, Master File lodgment and Australian Local File lodgment)	×	✓